ST 98-8
Tax Type: SALES TAX
Issue: Disallowed Resale Deductions (No Valid Certificates)
Failure To Verify Or Document Interstate Sales

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS

THE DEPARTMENT OF REVENUE OF THE STATE OF ILLINOIS	)	
v.	)	No. 95-ST-0000
	)	IBT 0000-0000
XYZ CORPORATION, INC.,	)	NTL SF-000000000000000
	)	John E. White,
Taxpayer.	)	Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Brian Wolfberg and Frederick Lochbihler of Schain, Firsel & Burney, Ltd., for taxpayer. Mark Dyckman and Marc Muchin, Special Assistant Attorneys General for the Illinois Department of Revenue.

Synopsis:

"XYZ" Corporation, Inc. ("XYZ" or "taxpayer") protested a Notice of Tax Liability ("NTL") the Illinois Department of Revenue ("Department") issued to taxpayer, which assessed retailers' occupation tax ("ROT") measured by gross receipts from transactions during the period from January, 1991 through the end of November, 1993.

Pursuant to a pre-hearing order, the parties agreed that two issues were to be resolved at hearing: (1) whether the transactions included in the Department auditor's schedule of global exceptions were sales or were loans; and (2) if the transactions were sales, whether they were sales for resale. At hearing, taxpayer and the Department

presented facts and evidence through stipulation. Taxpayer presented evidence through the testimony of its president, and through the testimony of the Department's auditor. The Department introduced "XYZ"'s returns filed during the audit period, some of its own audit records regarding "XYZ", and books and records obtained from "XYZ" during audit. I have considered the evidence adduced at that hearing, and I am including in this recommendation specific findings of fact and conclusions of law. I recommend the issue be resolved in favor of the Department.

Findings of Fact:

1. "XYZ" is a corporation engaged in business as an art gallery based in Chicago. Stipulation of Facts ("Stip."), ¶ 1. "XYZ" has specialized in the sale of American fine artworks, particularly paintings. *Id.* John Doe is the president and CEO of taxpayer. Hearing Transcript ("Tr.") p. 36.
2. "XYZ" files monthly returns with the Department as required by section 4 of the Retailers' Occupation Tax Act ("ROTA"), 35 **ILCS** 120/4. *See* Department Ex. 4 (copies of the monthly ROT returns filed by "XYZ" regarding the audit period). "XYZ" filed returns during each month of the audit period. *Id.*
3. The Department audited "XYZ"'s business for the period beginning January 1, 1991 and ending November 30, 1993. Department Ex. 1 (Department's correction of "XYZ"'s ROT returns, p. 2).
4. During his review of "XYZ"'s returns, the Department's auditor noted that "XYZ" claimed a high amount of deductions from taxable receipts as sales for resale. Department Ex. 5 (auditor's comments), p. 3; Department Ex. No. 4, *passim*.
5. "XYZ" did not keep documents conforming to section 2c of the ROTA (i.e.,

resale certificates, *see* 35 **ILCS** 120/2c) to support the deductions for receipts it claimed as being from its sales for resale. Department Ex. 5, p. 3.

6. After having the opportunity to obtain documents conforming to section 2c, "XYZ" obtained resale certificates from one gallery to whom it made several sales during the audit period. Department Exs. 2 (schedule of global taxable exceptions), 5. The Department allowed the deductions as claimed regarding the gross receipts "XYZ" received from sales to that gallery. Department Ex. 2, pp. 4-7 (entries for "TC").

7. The amount of tax at issue arises out of dozens of transactions (the "disputed transactions") which took place from approximately January 1, 1991 through February 28, 1993. Stip. ¶ 2.

8. The disputed transactions are included within the 627 exceptions the auditor identified in his schedules of global taxable exceptions. Department Ex. 2; *see also* Stip. ¶¶ 1-2.

9. During the audit, "XYZ" personnel provided the auditor with records of transactions – the disputed transactions – "XYZ" asserted were loans. Department Ex. 5, p. 2.

10. The parties' stipulation exhibit number 2 includes copies of documents respecting some but not all of the disputed transactions, which transactions the parties referred to as the "representative transactions." Stip. ¶ 3; Stip. Ex. 2. The parties stipulated that the representative transactions are representative of the disputed transactions, and that the documents from the representative transactions are representative of the documents in all of the disputed transactions. Stip. ¶ 4.

11. Stipulation exhibit 2 includes documents regarding each representative transaction, which documents include:

- copies of invoices (and most often a bill of sale) referencing a specific work of art and reflecting an amount given to "XYZ" by the other transacting party;
- copies of consignment agreement(s) between "XYZ" and the other transacting party;
- copies of letters from "XYZ" to the transacting party identifying a sum substantially higher than an invoice amount to be returned by "XYZ" to the other transacting party, and referring to post-dated checks included in the letter; and
- copies of some of the post-dated checks enclosed with "XYZ"'s letters.

Stip. Ex. 2; s*ee also* Stip. ¶ 3.

12. The documents contained in the parties' stipulated exhibit 2 identify eighty-nine (89) separate transactions. Stip. Ex. 2. The following list identifies each representative transaction by reference to the artwork identified by "XYZ"'s books and records, and by reference to the page numbers of the writings within stipulation exhibit 2.

Table 1: List of Representative Transactions

3-6	Designated Art	47-50	Designated Art	89-91	Designated Art
7-8	Designated Art	51-53	Designated Art	92-94	Designated Art
9-11	Designated Art	54-56	Designated Art	95-97	Designated Art
12-14	Designated Art	57-59	Designated Art	98-100	Designated Art
15-17	Designated Art	60-62	Designated Art	101-03	Designated Art
18-20	Designated Art	63-65	Designated Art	104-06	Designated Art
21-23	Designated Art	66-68	Designated Art	107-09	Designated Art
24-26	Designated Art	69-70	Designated Art	110-12	Designated Art
27-29	Designated Art	71-73	Designated Art	113-15	Designated Art
30-32	Designated Art	74-76	Designated Art	116-18	Designated Art
33-36	Designated Art	77-79	Designated Art	119-22	Designated Art
37-40	Designated Art	80-82	Designated Art	123-25	Designated Art
41-43	Designated Art	83-85	Designated Art	126-28	Designated Art
44-46	Designated Art	86-88	Designated Art	129-31	Designated Art

132-34 Designated Art	179-81 Designated Art	228-30 Designated Art
135-37 Designated Art	182-84 Designated Art	231-33 Designated Art
138-40 Designated Art	185-87 Designated Art	234-36 Designated Art
141-43 Designated Art	188-90 Designated Art	237-39 Designated Art
144-46 Designated Art	191-93 Designated Art	240-42 Designated Art
147-49 Designated Art	194-96 Designated Art	243-45 Designated Art
150-52 Designated Art	197-99 Designated Art	246-48 Designated Art
153-55 Designated Art	200-02 Designated Art	249-51 Designated Art
156-58 Designated Art	203-05 Designated Art	252-54 Designated Art
159-61 Designated Art	206-09 Designated Art	255-57 Designated Art
162-64 Designated Art	210-12 Designated Art	258-60 Designated Art
165-67 Designated Art	213-15 Designated Art	261-64 Designated Art
168-70 Designated Art	216-18 Designated Art	265-67 Designated Art
171-72 Designated Art	219-21 Designated Art	268-70 Designated Art
173-75 Designated Art	222-24 Designated Art	271-73 Designated Art
176-78 Designated Art	225-27 Designated Art	

Stip. Ex. 2.

13. Each invoice included in the parties' stipulation exhibit number 2 is a separately numbered form. Each bears "XYZ"'s preprinted name and address; the name and address of the other party to the transaction; the date of the transaction; the inventory number and description of a piece of art; and the cost of the artwork described. Each indicates that "XYZ" had received full payment for the artwork described on the invoice. *See, e.g.*, Stip. Ex. 2, pp. 3, 7, 9, 12. Each invoice also bears the words "FOR RESALE ONLY" or "NOT FOR DELIVERY – PURCHASED FOR RESALE", or some variant thereof.

14. On its ROT returns, "XYZ" reported the invoice amounts from the disputed transactions as receipts from either its sales for resale or as receipts from sales in interstate commerce. Department Exs. 2; 4 (page 2 of each return).

15. The Department's auditor determined that the receipts identified on the invoices "XYZ" kept and maintained regarding the disputed transactions should be included in "XYZ"'s taxable receipts. Department Exs. 5-6.

16. Although only three bills of sale are included in stipulation exhibit number 2

(Stip. Ex. 2, pp. 4, 34, 38), the parties stipulated that each representative transaction involved documentation including, most often, a bill of sale. Stip. ¶ 3.

17. Printed near the top of each bill of sale is the following sentence: "XYZ", Inc., hereby sells and transfers to the Customer identified below, the works of art described below; all subject to the terms and conditions contained herein, including those set out on the reverse side hereof." Stip. Ex. 2, pp. 4, 34, 38.[1]

18. Printed near the bottom of each bill of sale, just above the place for the customer's signature, is the following sentence: "I (We), the Customer, have read and understand this Bill of Sale and the terms and conditions on the reverse side. I (We) have examined the work(s) of art and find it to be in accordance with the description above and I (we) acknowledge delivery and receipt." Stip. Ex. 2, pp. 4, 34, 38.

19. One of the bills of sale included in the exhibit is signed by both John Doe and the customer (Stip Ex. 2, p. 38), one is signed by the customer only (*id.*, p. 4) and one is signed by John Doe only (*id.*, p. 34).

20. "XYZ" contends that the invoices and the bills of sale were used to document how much money "XYZ" was borrowing from the other transacting party in the disputed transactions. *See* Tr. pp. 51-52 (Richard "XYZ").

21. Each Consignment Agreement bears "XYZ"'s preprinted name and address and the name and address of the consignor. The consignor named on each consignment agreement is also the party named in the accompanying invoice; and, the parties stipulated, on the bills of sale often completed with the invoices. The

dates of the consignment agreements correspond with the dates of the invoices. Each consignment agreement included in stipulation exhibit 2 contained the following pre-printed provisions:

> **In consideration of the mutual promises and undertakings as hereinafter set out, the parties hereto agree as follows:**
>
> 1. Consignor hereby consigns for sale to Gallery on the terms hereinafter set out, the work or works of art set out and listed on Exhibit "A" below hereof, (said work or works of art are hereinafter called "works"), and Gallery acknowledges receipt of the works as of the date of this Agreement.
>
> 2. Consignor hereby warrants and represents that he is the sole owner of all the works listed on Exhibit "A". Consignor further warrants and represents that all of the works are unencumbered and free from liens, or claims against them from any person.
>
> 3. Gallery agrees to use reasonable and bona fide efforts to sell the works. It is understood and agreed between the parties that Gallery, at its sole discretion, will determine the manner, method and time of sale which will have the most beneficial affect upon the ultimate valuation of the works. Gallery shall receive as its commission hereunder, and Consignor shall receive as his compensation, the sum or sums as follows:
>
> * * *
>
> Consignor shall be paid his share as soon as practicable after the sale has been consummated and the purchase price received by Gallery.
>
> 4. Gallery may advertise, promote, exhibit and/or publish any information or photograph it deems necessary either by itself or through others, regarding the works, the artist, or any other matter Gallery deems relevant.
>
> **EXHIBIT "A"**
>
> [description of artwork]
>
> **This Agreement is subject to the conditions, agreements and stipulations contained on the reverse side of this page.**

[1] The parties did not include a copy of the reverse side of any bill of sale included in the representative transactions in their stipulated exhibit number 2. *See* Stip. Ex. 2.

> **IN WITNESS WHEREOF, the parties hereto have executed this Agreement the day, month and year first written above.**

E.g., Stip. Ex. 2, pp. 5, 10, 35.

22. Many of the consignment agreements are executed by "XYZ", through either the handwritten or stamped signature of its president. *See* Stip. Ex. 2. None of the consignment agreements were executed by the named consignors. *Id.*

23. Paragraph 3 of each consignment agreement includes a typed description of how the Gallery's commission and the consignor's compensation would be paid. For example: "Consignor shall receive one hundred eight thousand dollars ($108,000) from the sale of the work listed in Exhibit 'A'. Gallery to receive remainder of the selling price as its commission" (Stip. Ex. 2, p. 5); "Consignor shall receive $48,000 from the sale of the work listed in Exhibit A. Gallery to receive remainder as commission" (*id.*, p. 10); "Consignor shall receive a net amount of $44,500 from the painting listed in Exhibit A" (*id.*, p. 16); "Consignor shall receive $27,000 from the sale of the painting listed in Exhibit A. Gallery shall retain the balance as its commission" (*id.*, p. 25).

24. Of the eighty-five consignment agreements included in stipulation exhibit 2, 65 refer to the consignor's compensation as being, in substance if not verbatim, "from the sale of the work listed in Exhibit A." *See* Stip. Ex. 2.

25. The table below lists the page numbers of each consignment agreement included in the parties' representative transactions exhibit. *See* Stip. Ex. 2. The table classifies each consignment agreement by whether ¶ 3 of each refers to the "sale"

(or some variant thereof)[2] of the artwork putatively consigned to "XYZ".

Table 2: Terms Used in Consignment Agreement ¶ 3:

"Sale" referred to in consignment ¶ 3	**"Sale" not referred to in ¶ 3**
5, 10, 22, 25, 28, 31, 35, 39, 42, 45, 48, 52, 55, 58, 61, 87, 108, 111, 114, 117, 120, 124, 127, 130, 133, 136, 139, 142, 145, 148, 151, 154, 157, 160, 163, 166, 169, 174, 177, 180, 183, 186, 189, 192, 195, 198, 201, 204, 207, 211, 214, 217, 220, 223, 226, 232, 235, 238, 241, 244, 247, 250, 253, 256, 269,	13, 16, 19, 65, 67, 72, 75, 78, 81, 84, 90, 93, 96, 99, 105, 229, 259, 262, 266, 272

Stip. Ex. 2. There were no consignment agreements included in the representative transactions for the works titled, "Designated Art (A)" (Stip. Ex. 2, pp. 7-8), "Designated Art (B)" (Stip. Ex. 2, pp. 69-70) and "Designated Art (C)" (Stip. Ex. 2, pp. 171-72).

26. The parties' stipulation exhibit 2 includes a copy of a letter (in some instances, two letters) from "XYZ" to the other transacting party regarding the representative transaction. Stip. Ex. 2. Most, but not all of the letters bear the same date as the invoice, bill of sale and consignment agreement included as documentation representative of the disputed transactions. *See* Stip. Ex. 2, pp.

[2] For example, the consignment agreement on page 39 provides: "Consignor to receive twenty-two thousand five hundred dollars ($22,500) from the work listed in Exhibit 'A'. Gallery

119-22, 150-52.

27. John Doe signed most of the letters in stipulation exhibit 2. Stip. Ex. 2.

28. Jane Doe, John's wife, and the person who prepared and signed the ROT returns for "XYZ" during the audit period (Department Ex. 4), also signed letters included in the representative transactions exhibit. Stip. Ex. 2, pp. 50, 122; *see also* Tr. pp. 36-37, 59, 67 (Jane Doe is a shareholder of "XYZ", and worked as bookkeeper for "XYZ" during the audit period). Jane Doe's signed name appears on most but not all of the post-dated checks contained in the representative transactions exhibit. Stip. Ex. 2, pp. 94, 106, 167, 209.

29. Each of the post-dated checks contained in the representative transactions exhibit contains a section labeled "in payment for". Stip. Ex. 2, pp. 94, 106, 167, 209. On one of the checks included in the representative transactions exhibit, the "in payment for" section contains the inventory number (R-257) of the painting identified in the invoice, consignment agreement and letter "XYZ" created and kept to document that disputed transaction. Stip. Ex. 2, pp. 104 (invoice), 105 (consignment agreement), 106 (letter from "XYZ").

30. The language "XYZ" used in each letter varies. The table below identifies the page numbers of all of the letters included in Stipulation Exhibit 2. The table classifies each letter by whether "XYZ" referred to each representative transaction as involving a "sale", "purchase" or "acquisition" of artwork.

Table 3: Terms Used in "XYZ"'s Letters:

"Sale" "purchase" or "acquisition" of artwork referred to in letter	**"Sale/purchase/acquisition" not referred to in letter**

to receive remainder of *selling price* as its commission." Stip. Ex. 2, p. 39 (emphasis added).

6, 8, 11, 14, 17, 20, 23, 29, 32, 36 40, 43, 46, 49, 53, 59, 62, 64, 68, 70, 73, 76, 79, 82, 85, 88, 91, 94, 97, 100, 102, 109, 112, 121, 125, 131, 134, 137, 140, 143, 146, 149, 158, 161, 164, 167, 170, 172, 175, 178, 181, 184, 187, 190, 193, 196, 199, 202, 230, 233, 236, 239, 242, 245, 248, 251, 254, 257, 260, 263-4, 267, 270, 273	26, 50, 56, 106, 115 118, 128, 205, 208, 212 215, 218, 221, 224, 227

Stip Ex. 2.

31. In seventy-four of the representative transactions, the letter from "XYZ" refers to the purchase, sale or acquisition of the artwork identified in the invoice, bill of sale and/or consignment agreement. Stip. Ex. 2; Table 3, *supra*, p. 10. In thirteen of the fourteen representative transactions in which the letter from "XYZ" did not use the word "sale" (or some variant thereof), ¶ 3 of the corresponding consignment agreement referred to the "sale" of the artwork. Table 3, *supra*, p. 10.

32. In only one of the representative transactions does neither the letter from "XYZ" nor ¶ 3 of the consignment agreement refer to a sale of the artwork identified in the corresponding invoice. *See* Stip. Ex. 2, pp. 104-06 (documents regarding "Designated Art (D)" by XXXX). Paragraph 3 of the consignment agreement for that representative transaction provides, "Consignor shall receive $17,500 as net return on the painting listed in Exhibit 'A.'" *Id.* at 105.

33. Two of the eighty-nine representative transactions involve the transfer, or putative transfer, of the same piece of art to two separate purchasers/lenders. Stip. Ex. 2, pp. 9-11, 219-221 (work titled, "Designated Art (E)").

34. The second time "XYZ" either sold "Designated Art (E)," or took a loan from a customer and referenced that loan with documents in which it purported to sell that painting, the invoice price was significantly higher than the first transaction involving the same work. Stip. Ex. 2, pp. 219-221 (invoice indicating "XYZ" sold the painting on 2/26/92 for $20,000, with consignment for $25,000), pp. 9-11 (invoice indicating "XYZ" sold the painting on 10/27/92 for $39,000, with consignment for $48,000).

35. The invoice amounts from the disputed transactions make up a large percentage of the "Total Receipts" "XYZ" reported in box 1 of its ROT returns. For example:

- During 1991, "XYZ" reported that it had receipts from sales of tangible personal property[3] in excess of $15,800,000. Department Ex. 4, pp. 1-26; *see also*, Table 4, *infra*, p. 14.[4] Approximately $9,348,000 of that amount was attributable to the amounts identified on the invoices "XYZ" created to document the disputed transactions. Table 4 *infra*, p. 14 (detailing information reported by "XYZ" and made part of the record in Department Exs. 2 and 4).
- During 1992, "XYZ" reported receiving approximately $26,000,000 in receipts from selling goods. Department Ex. 4, pp. 27-54; Table 4, *infra*, p. 14. Approximately $9,000,000 of that amount was attributable to the invoice amounts for the disputed transactions. Table 4, *infra*, p. 14.

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[3] For each year of the audit period, "XYZ" reported slightly less than $30,000 from its sales of service, for a total of approximately $83,700. Department Ex. 4 (page 2 of each return filed); Table 4, *infra*, p. 15 (receipts from "XYZ"'s sales of service as reported detailed). "XYZ" reported those receipts as being from its sales of repair services, shipping or freight.

[4] Table 5 was created using information contained in Department Ex. 4 ("XYZ"'s returns as filed) and Department Ex. 2 (global taxable exceptions).

- During the audit period, "XYZ" reported that it realized approximately $51,000,000 in receipts from selling goods. Department Ex. 4; Table 4, *infra*, p. 14. Approximately $19,000,000 of that amount is attributable to the invoice amounts for the disputed transactions.

36. Table 5, *infra*, p. 15, measures the difference between the invoice price and the consignor's compensation amount as set forth in ¶ 3 of the consignment agreement kept regarding each representative transaction. The consignor's compensation equaled the amount of the post-dated checks referred to in the letter(s) "XYZ" wrote to the putative purchaser/consignor regarding each representative transaction. Stip. Ex. 2, *passim*.

37. Table 5, *infra*, p. 15, also quantifies as a percentage of the invoice price what "XYZ" generally referred to in the letters included in Stip. Ex. 2 as the "return" agreed to by the parties. Table 5, *infra*, p. 15; Stip. Ex. 2, p. 106. The return to the other transacting party in each representative transaction ranged from 6% over the course of 1 month (Stip. Ex. 2, pp. 173-75) to 100% over the course of 9 months. Stip. Ex. 2, pp. 101-03. The column entry in Table 5 for "No. of months from invoice to full return / loan period" refers to the number of calendar months between the date of the invoice to the month during which the last post-dated check referred to in "XYZ"'s letter was to be deposited.

38. The invoice prices from the disputed transactions equaled approximately $9,000,000 during each of the first two years in the audit period, and approximately $650,000 during the last eleven months of the audit period. Department Ex. 2 (global taxable exceptions); Table 5, *infra*, p. 15. .

39. The invoice amounts for all of the disputed transactions claimed to be loans equal $19,019,413. Table 4, *infra*, p. 14.

40. "XYZ" did not introduce its corporate income tax returns filed regarding the audit period as evidence at hearing.

Conclusions of Law:

The *prima facie* correctness of the Department's action in this matter was established when the Department's correction of "XYZ"'s returns was introduced at hearing under the certification of the Director. 35 **ILCS** 120/4. The Department's *prima facie* case is overcome, and the burden shifts to the Department to prove its case, when a taxpayer presents evidence that is consistent, probable and identified with its books and records, to show that the Department's corrected returns are not correct. Copilevitz v. Department of Revenue, 41 Ill. 2d 154, 156-57 (1968).

Issue 1:

The key issue in this matter is whether the disputed transactions were sales of tangible personal property on which retailers' occupation tax is properly measured. The Department contends that the gross receipts "XYZ" recorded on the invoices it made regarding the disputed transactions should measure "XYZ"'s ROT liability. *See* Stip. ¶ 2. "XYZ" contends that since the disputed transactions represent financing techniques or loans and not sales of tangible personal property for use or consumption, the receipts from those transactions should not be included in its taxable gross receipts. *See id.*

"XYZ" contends the transactions were not sales of tangible personal property at retail because the documents introduced as a stipulated exhibit establish that the transactions were not sales "for use or consumption." Post-Hearing Memorandum of Taxpayer, "XYZ" Galleries, Inc. (""XYZ"'s Memo"), p. 1. Instead, "XYZ"'s argument continues, the stipulated documents show that the transactions involved loans of money from persons to "XYZ", which "XYZ" documented with writings referring to artwork from its inventory. *See* i*d.*, 1-2. Specifically, "XYZ" argues that:

> [t]he transactions arose out of "XYZ"'s need to obtain financing to fund a major expansion, and its ability to borrow from typical business and commercial lenders. "XYZ" instead borrowed from wealthy clients, offering rates of return substantially higher than the returns enjoyed by typical lenders. Attempting to document these loan transactions without the assistance of counsel, John Doe, the art dealer who owned "XYZ", cobbled together an integrated contract comprised of a bill of sale and/or invoice to evidence the amount of money "XYZ" received as a loan, a consignment agreement to evidence the amount of money that "XYZ" would repay the lender for the loan plus interest, and a letter and postdated checks, which effectively identified the terms for the repayment of the loan. He [i.e., "XYZ"'s president] structured each loan with some relation to a specific work of art, both to provide "some comfort" to lenders about "XYZ"'s asset base, and to help the gallery make certain it did not borrow more than could be repaid through a sale of inventory. The key was the postdated checks component, which evidenced "XYZ"'s unconditional obligation to repay the loan plus interest. The creditors never took possession of any artwork, and took no risk tied to the sale of the artwork or the fluctuation of its market value.

"XYZ"'s Memo, pp. 1-2.

Initially, the Department counters by reiterating the statutory presumption of correctness that attaches to its correction of "XYZ"'s returns. It also argues that "XYZ" reported the transactions as sales on the ROT returns it filed with the Department,[5] and it documented the transactions as sales on the books and records it maintained in the regular course of its business. Department's Post-Hearing Brief ("Department's Response"), pp. 2-3. The Department argues that the testimony of "XYZ"'s president cannot overcome the statutory presumption of correctness that attaches to its correction of "XYZ"'s

[5] "XYZ" reported the receipts from the disputed transactions as either sales for resale or sales in interstate commerce. The receipts from either such transactions are deductions from taxable gross receipts. "XYZ" neither charged nor collected ROT on the disputed transactions.

returns, because his testimony is inconsistent with the books and records "XYZ" stipulated were representative of all the transactions at issue. *Id.*

Since both parties argue the books and records in evidence undercut their opponents' claims regarding the disputed transactions, I will address those records. Included as an exhibit to the parties' stipulation of fact are 270 (two hundred seventy) pages of documents, each of which generally fall into one of three categories. The three types of documents include an invoice (and most often, a bill of sale), a consignment agreement, and a letter from "XYZ". Stip. ¶ 3; Stip. Ex. 2.

In each letter included in the exhibit, "XYZ" referred to post-dated checks which, the Department does not dispute, were enclosed with each letter sent to the putative purchaser/lender. In most, if not all, of the letters included in the representative transactions exhibit, "XYZ" informed each addressee to deposit the checks enclosed on the date stated on the check. These post-dated checks, "XYZ" contends, present the most compelling evidence that the transactions were not sales of tangible personal property, but were instead loans of money to "XYZ" from the putative purchasers. In response to "XYZ"'s contention, the Department argues that the post-dated checks "XYZ" tendered with the paperwork already described "are essentially worthless and do not create a loan." Department's Response, p. 10.

The significance of the post-dated checks within the different writings "XYZ" kept and maintained regarding the disputed transactions is that "XYZ" apparently agreed to pay the putative purchaser/consignors before, or regardless whether, the art consigned was sold by "XYZ". Notwithstanding the Department's discount of the instruments as evidence here, they offer some documentary support for "XYZ"'s claim that the disputed

transactions may have been undertaken pursuant to unwritten loan agreements. What remains is a determination regarding what those post-dated checks represented. Did they represent "XYZ"'s payment of the return it guaranteed to each transacting party for its purchase and consignment of the artwork identified in the writings "XYZ" created to document the disputed transactions? Or, did they represent "XYZ"'s guaranteed repayment of an unwritten loan agreement, the terms of which had nothing to do with the item of artwork identified in the writings "XYZ" gave to each party, as part of that agreement?

The Illinois Supreme Court long ago recognized that "there is no more convincing evidence of what the parties [to a contract] intended than to see what they did in carrying out its provisions." Department of Revenue v. Jennison-Wright Corp., 393 Ill. 401, 408 (1946). Proof of facts probative of the issue presented here called out for evidence regarding how the parties acted toward, or how they treated, both the monies exchanged and the tangible personal property involved with the disputed transactions. Even considering the checks and Richard "XYZ"'s testimony, I cannot conclude that "XYZ" rebutted the presumption of correctness afforded the Department's correction of "XYZ"'s returns. "XYZ" did not rebut the Department's *prima facie* case because "XYZ"'s evidence was inconsistent with the other evidence of record, including "XYZ"'s own books and records, admitted at hearing.

The first inconsistency lies in John Doe's testimony regarding the writings "XYZ" created and maintained regarding the disputed transactions, and his understanding of the unwritten agreement he asserts existed regarding those transactions. Before I discuss the testimony itself, it is important to recall why parol evidence was admissible

here. Assuming the disputed transactions were transactions involving goods, and the U.C.C. applies, parol evidence was admissible to help determine whether the agreement was completely or partially integrated,[6] and to explain the meaning of the agreement, even if it were fully integrated. J & B Steel Construction v. C. Iber & Sons Inc., 162 Ill. 2d 265, 273 (1994); Arcor Inc. v. Textron, Inc., 960 F.2d 710, 715-16 (7th Cir. 1992) (*citing* 810 **ILCS** 5/202(b) and recognizing that, "… it is the writing, not the agreement itself, that may be supplemented by evidence of consistent additional terms"). I cannot conclude that the writings included in the representative transactions exhibit are a complete and final expression of the agreement between "XYZ" and the transacting parties. Since the writings are, at most, an incomplete expression or partial integration of the agreement, parol evidence of additional, consistent terms was admissible to supplement or explain the terms included in the different writings "XYZ" used to express that agreement. J & B Steel, 162 Ill. 2d at 273.

The only way the writings "XYZ" used to document the disputed transactions can be understood to have been created and used to document a loan is if those writings were intended to create a security interest in the goods identified therein in favor of the other transacting parties. *See* 810 **ILCS** 5/1-201(37) ('"Security interest' means an interest in personal property or fixtures which secures payment or performance of an obligation"). That point was perfectly described within "XYZ"'s responsive memorandum to the Department's Motion in Limine. "XYZ" filed that memorandum to oppose the Department's attempt to prevent "XYZ" from offering parol evidence to explain the

[6] The integration question actually involves two questions: (1) is the writing a final expression of the agreement between the parties? and (2) is the writing a complete expression of the agreement between the parties? J & B Steel, 162 Ill. 2d at 272-73.

terms of the different contracts and writings (e.g., the invoices, bills of sale, consignment agreements, letters, etc.) "XYZ" used to document the disputed transactions. "XYZ"'s Reply to the Department's Motion in Limine, p. 6 (*quoting* UCC Comment 4 to 810 **ILCS** 5/9-203). But at hearing, John Doe did not explain or supplement the terms of the invoices, bills of sale and consignment agreements. Instead, he testified as follows:

> Q: Why was art involved at all?
> Why did you mention any art at all in these documents?
> A: That is what I buy and sell. I don't buy and sell other things. I don't sell widgets.
> We had a very large Gallery for a while, three galleries; and we had a – I call it an asset base, and that is the way in which we memorialized these loan transactions.
> I think maybe it gave them some comfort to know that what we had there was available for sale, but it was our whole business system to which they look for repayment.
>
> Q: So are you saying that particular pictures or works of art that are mentioned there, were not collateral for particular loans?
> A: Not particular pictures.
> I think that the overall inventory of "XYZ" was certainly seen as something solid and big and viable at this time, but not the specific pictures as collateral.

Tr. pp. 56-57 (John Doe).

Even if Mr. Doe were competent to testify as to what the other transacting parties understood regarding the writings he decided to use to document the disputed transactions (*see* Tr. pp. 48-49, 55-57) his own understanding of them is inexplicable. The substance of his testimony was that all of the different terms or provisions in the writings which referred to the sale, purchase, or return due from the sale of the items of artwork, were meaningless. Under Mr. Doe's understanding of the agreements, the bills of sale are entirely worthless. His testimony contradicts the only seemingly rational

explanation why writings which purport to transfer ownership of goods should be understood to describe loan transactions. *See* 810 **ILCS** 5/9-203 (comment 4). Parol evidence cannot be used to contradict the terms expressed in the writings the parties included in an agreement involving transactions in goods — even writings which comprise only an incomplete expression, or partial integration, of the agreement between them. J & B Steel, 162 Ill. 2d at 273.

Second, it is hard to review the documents included in the parties' stipulated exhibit and not conclude that, if the disputed transaction were always intended to be loans, the parties must have also intended to make the transactions appear to be short term speculations in artwork. "XYZ" used invoices and bill of sale on which he recorded putative transfers of the artwork identified in those documents to the other transacting party. "XYZ" used consignment agreements ordinarily used when it took an item of artwork into its custody intending to sell it for the owner. *See* Tr. p. 51 (John Doe). "XYZ" completed and sent letters to the other transacting parties in which he described the consignor's compensation as the return the other transacting party was to receive from "XYZ"'s sale of the artwork putatively consigned.

Taken together, those writings show that the disputed transaction did not merely involve one person's tender of "money in exchange for post-dated checks … in an amount substantially greater than the amount given." "XYZ"'s Reply, p. 4. If the only documents in evidence were "XYZ"'s post-dated checks, that description of the transactions might be appropriate. Instead, the writings show that the disputed transactions involved "XYZ"'s tender of: (1) documents transferring title to tangible personal property (i.e., the invoice and bill of sale); (2) a document allowing "XYZ" to

maintain possession of the property transferred and requiring "XYZ" to use reasonable and bona fide efforts to sell the property for an agreed amount of return to both the title holder and to "XYZ" (the consignment agreement); and, (3) a letter and post-dated drafts in an amount equal to the return stated in the consignment agreement. In exchange, the other parties tendered: (1) the invoiced price of the property; and (2) their (implied) promise to deposit the post-dated checks on the dates written thereon.

While "XYZ" tried to have the Department's auditor "admit" that the disputed transactions fit a California court's definition of a "loan" (*see* Tr. pp. 19-29 (Witness); "XYZ" Offer of Proof Ex. 1), Illinois law has been relatively clear that "a sale is a transfer of title in exchange for consideration." Wheeler v. Sunbelt Tool Co., 181 Ill. App. 3d 1088, 1098 (*citing* Burrus v. Itek Corp., 46 Ill. App. 3d 350, (1977)). "XYZ"'s letters show that the transacting parties' receipt of documents purporting to transfer title to artwork was part of the bargain. Stip. Ex. 2, pp. 70, 76, 79, 82, 100.

There are rational explanations why persons might agree to make a loan look like a sale of property. For one, the lender might well be more amenable to make a loan when he receives, as part of the agreement, documents which, on their face, purport to transfer title to a valuable item of collateral to the lender. For another, by disguising a loan as a sale of property to the lender, coupled by an immediate consignment of the property to the borrower for subsequent sale by the borrower, the lender has purchased documents with which it might claim that the income received for use of the money loaned was instead a short-term gain from the lender's speculation in a given type of property. To persons in higher tax brackets, which Mr. "XYZ" generally described the other parties to the disputed transactions (Tr. pp. 49), income from capital gains, even short-term gains,

might be taxed at a lower rate than ordinary interest income. *See* 26 U.S.C. § 1(a), (j) (1991).

And for persons in the borrower's position, such as "XYZ", an agreement to disguise loans as sales might have two potentially positive effects.[7] First, the borrower could claim an increased level of sales, or a greater level of creditworthiness. A retailer claiming annual sales of 15 or 26 million dollars might be in a better position to obtain financing for a capital acquisition, such as a particularly attractive piece of real property, than would a retailer who could claim annual sales of, let's say, 6 or 16 million dollars. *See* Table 4, *supra*, p. 14. Second, and especially where the value of the goods identified to the contracts is subjective (*see* Tr. pp. 45-47, 63), the retailer could show a downstream purchaser that the market value of a specific good increased by a certain percentage over the last few months or years.

Whether that was what happened when "XYZ" either sold "Designated Art," or took a loan and referenced that loan with documents in which it purported to sell that painting twice in the same calendar year, the second time for a price almost twice as much as the first time, is not disclosed by the evidence of record. Nor is there any evidence regarding how the other transacting parties treated the returns "XYZ" guaranteed regarding the putative purchases and consignments of artwork. What is disclosed by the record, however, is the way "XYZ" treated the amounts it recorded as the invoice prices of the artwork identified in the disputed transactions. *Compare* Department Ex. 2 *with* Department Ex. 4; *see also* Table 4, *supra*, p. 14; Tr. p. 59-60

[7] The utility of such a disguise to the borrower (if it were a disguise), however, would necessarily depend on whether the borrower could reveal the true character of the agreement come tax time.

(John Doe). On the ROT returns "XYZ" filed during the audit period, "XYZ" reported those invoice prices as part of the receipts it earned from selling tangible personal property. Department Exs. 2, 4; Tr. pp. 59-60, 62 (John Doe).

In stark contrast with the writings "XYZ" used to document the disputed transactions, "XYZ" was perfectly able to express, in writing, that it received a loan from someone, without resort to documents such as bills of sale and consignment agreements. Specifically, Department exhibit number three is a copy of a letter on "XYZ"'s letterhead, signed by John Doe, which stated:

> This letter concerns a Loan received in the amount of $10,000 (wire and check).
> Our agreement was that you receive a return of $15,000 on August 2, 1993 and I have enclosed that check for you as my guarantee.

Department Ex. 3.

That letter was written during the audit period. "XYZ" did not refer to an item of artwork, or to an invoice or a consignment agreement in that letter. Nor was there any evidence suggesting that "XYZ" included the $10,000 it borrowed in October 1992 as part of its total receipts on the ROT return filed for that month. *See* Department Ex. 2, pp. 13-14 (loan from "Person" Department Ex. 3, not included in the schedule of global taxable exceptions for 10/92). In short, and even without help from counsel, "XYZ"'s president and CEO knew how to articulate when his company received a loan from someone. Moreover, where "XYZ" received funds from someone pursuant to an agreement it described simply as a loan, it didn't report such amounts as having come from its sales of tangible personal property. Given "XYZ"'s own treatment of the invoiced amounts from the disputed transactions, it is not inconceivable that "XYZ" may

have treated those transactions as short-term, low-risk speculations in artwork, because that is what the disputed transactions were always intended to be.

To be sure, if the disputed transactions were loans, "XYZ" committed a gross error by reporting the invoice prices as part of its total receipts from selling tangible personal property on its monthly ROT returns. At hearing, John Doe couldn't explain why his company reported those invoice prices as sales receipts. Tr. pp. 59-60 (John Doe). He seemed to blame that error on the unsophisticated bookkeeping capabilities of his wife, who prepared and signed the ROT returns filed during the audit period. *Id*.; *see also*, "XYZ"'s Reply, p. 5. Mrs. Doe, however, appears to have had personal knowledge of the disputed transactions. At least, she signed some of the letters the parties included in the representative transactions exhibit. Stip. Ex. 2, pp. 50, 122. Unless Mrs. Doe, the second of the two corporate shareholders of "XYZ", the wife of "XYZ"'s president and CEO, and "XYZ"'s bookkeeper, was wholly ignorant of any unwritten agreements pursuant to which the disputed transactions were made, she could not have been acting "open and straightforward" by regularly reporting those loan amounts as the corporation's receipts from selling tangible personal property. *See* Tr. pp. 59-60 (John Doe). Since Jane Doe did not appear as a witness at hearing, the reasons why she reported the invoiced amounts from the disputed transactions as sales receipts, as well as any personal knowledge she may have had regarding those transactions, remains unclear.

There was another way in which "XYZ" did not treat the disputed transactions as loans. The Internal Revenue Code requires corporations to issue certain forms (i.e., 1099 forms) to document their payment of interest in excess of $10 annually. *See* 26 U.S.C. § 6049(a)(1)(1991). "XYZ", however, did not issue such forms to the other parties to the

disputed transactions. Tr. pp. 63, 65 (Richard "XYZ"). The Department argued that "XYZ"'s failure to issue 1099's shows that the disputed transactions were sales and not loans. Department's Response, p. 5. More appropriately, John Doe's admission on this point shows that "XYZ" did not act as though it was paying interest on outstanding indebtedness.

Even though "XYZ" failed to issue the appropriate tax forms to the persons from whom it claims to have taken loans instead of making sales, "XYZ" could have still shown that it treated the disputed transactions as loans by introducing its federal income tax forms for the tax years during the audit period. If "XYZ", in fact, committed consistent and gross errors by reporting the amounts of money it borrowed as receipts from selling property on its ROT returns for a good portion of the audit period, it should not have compounded those errors by similarly reporting such monies as receipts from sales on its federal income tax returns. "XYZ"'s federal income tax returns would have reflected whether "XYZ" treated the amounts it recorded on the disputed transaction invoices as either loan receipts or as receipts from sales for income tax purposes.

If the disputed transactions were loans, then "XYZ"'s reported "gross receipts or sales" in box 1a of its 1991 federal form 1120 (U.S. Corporation Income Tax Return), should have been closer to $6,500,000 (total ROT receipts minus the invoice prices of the disputed transactions) than the $15,800,000 it reported in all of its ROT returns filed for that year. Department Ex. 4; Table 4, *supra*, p. 14. Similarly, the amount "XYZ" reported in box 1a of its 1992 return should have been closer to $16,900,000 than the $25,900,000 it reported on the ROT returns filed regarding that year. Table 4, *supra*, p. 14.

Moreover, if the amounts "XYZ" referred to as the "return" it guaranteed to the other transacting parties were, in reality, the amounts of interest "XYZ" paid for the use of the money it borrowed, then "XYZ" should have reported those significant amounts to the IRS as the interest expenses it incurred during the pertinent years in box 18 of its federal corporate income tax returns. *See* 26 U.S.C § 163 ("There shall be allowed as a deduction all interest paid or accrued within the taxable year on indebtedness."). The average return per representative transaction was approximately 29% of the invoice price for each such transaction. *See* Table 5, *supra*, p. 15. If the disputed transactions were, in fact, loans, then "XYZ" would have paid approximately 29% of the invoice prices from the disputed transactions as interest on those loans. Stip. ¶ 4 (the representative transactions are representative of the disputed transaction").

For 1991, "XYZ" should have been able to claim a deduction of approximately $2,710,000 for the interest to be imputed to the disputed transactions. *Compare* Tables 4-5, *supra*, pp. 14-15 (29% of $9,348,100, i.e., the invoice price totals of the disputed transactions, equals $2,710,949). For 1992, "XYZ" should have been able to claim a deduction of approximately $2,610,000 for the interest to be imputed to the disputed transactions. *Id.* (29% of $9,019,813 equals approximately $2,615,746). For the audit period, the interest to be imputed to the disputed transactions would be roughly $5,500,000. *Id.* (29% of $19,019,413 equals approximately $5,515,630). "XYZ", however, did not introduce its income tax returns filed regarding the audited tax years. The record, therefore, does not show how "XYZ" treated the monies associated with the disputed transactions for income tax purposes.

"XYZ" did not introduce credible evidence of consistent additional unwritten

terms to explain or supplement the writings it used to document the disputed transactions. *See* J & B Steel Construction v. C. Iber & Sons Inc., 162 Ill. 2d at 273; Arcor Inc. v. Textron, Inc., 960 F.2d 710, 715-16 (7th Cir. 1992). The parol evidence "XYZ" introduced to support its claim that the disputed transactions were undertaken pursuant to unwritten loan agreements contradicted the terms of the writings it used to document those transactions, and it was also inconsistent with its own treatment of monies associated with the disputed transactions. Therefore, I conclude that "XYZ" has not rebutted the *prima facie* correctness of the Department's determination that those transactions were sales upon which tax should be measured.

Issue 2:

If the disputed transactions were sales of tangible personal property instead of loans, the parties contested whether such sales were sales for resale.

Section 1 of the ROTA provides, in part:

> *"Sale at retail" shall be construed to include* any transfer of the ownership of or title to tangible personal property to a purchaser, for use or consumption by any other person to whom such purchaser may transfer the tangible personal property without a valuable consideration, and to include *any transfer, whether made for or without a valuable consideration, for resale in any form as tangible personal property unless made in compliance with Section 2c of this Act.*

35 **ILCS** 120/1 (emphasis added).

Section 2c of the ROTA provides, in part:

> Except as provided hereinabove in this Section, a sale shall be tax-free on the ground of being for resale if the purchaser has an active registration number or resale number from the Department and furnishes that number to the seller in connection with certifying to the seller that any

> sale to such purchaser is nontaxable because of being a sale for resale.
>
> *Failure to present an active registration number or resale number and a certification to the seller that a sale is for resale creates a presumption that a sale is not for resale.* This presumption may be rebutted by other evidence that all of the seller's sales a sales for resale, or that a particular sale is for resale.

35 **ILCS** 120/2c (emphasis added).

Finally, section 7 of the ROTA provides, in part:

> To support deductions ... authorized under this Act, on account of receipts from ... sales of tangible personal property for resale, ... entries in any books, records or other pertinent papers or documents of the taxpayer in relation thereto shall be in detail sufficient to show the name and address of the taxpayer's customer in each such transaction, the character of every such transaction, the date of every such transaction, the amount of receipts realized from every such transaction, and such other information as may be necessary to establish the nontaxable character of such transaction under this Act. * * *
>
> * * *
>
> *It shall be presumed that all sales of tangible personal property are subject to tax under this Act until the contrary is established,* and the burden of proving that a transaction is not taxable hereunder shall be on upon the person who would be required to remit the tax to the Department if such transaction is taxable. * * *

35 **ILCS** 120/7 (emphasis added).

If the disputed transactions were, in fact, sales of tangible personal property instead of loans, "XYZ" has failed to rebut the presumption that tax was due in the amount identified by the Department. In fact, "XYZ"'s argument is similar to the argument rejected by the Illinois supreme court in Tri-America Oil Co. v. the Department of Revenue, 102 Ill. 2d 234, 240 (1984). In that case, Tri-America Oil Co., a retailer and wholesaler of gasoline, was assessed ROT on sales of gasoline it made to an unregistered

gasoline station. Even though that purchaser could not and did not provide Tri-America with its registration number and a certification that its purchases were for resale, Tri-America sold it gasoline without charging retailers' occupation tax on the selling price thereof.

Tri-America first argued that it was exempt from retailers' occupation taxes pursuant to the Illinois supreme court decisions in Dearborn Wholesale Grocers, Inc. v. Department of Revenue, 82 Ill. 2d 471 (1980) and Illinois Cereal Mills, Inc. v. Department of Revenue, 99 Ill. 2d 9 (1983). Tri-America Oil Co., 102 Ill.2d at 238. The court disagreed, finding that Tri-America held itself out to the public a retailer by operating three gas stations, and also finding that Tri-America's sales to the unregistered "reseller" were both regular and substantial. *Id.*, at 239. The court also concluded that section 2c was intended to do more than just provide the retailer with the means for supporting a specific of deduction from its taxable gross receipts. The court wrote:

> The taxing statutes are designed to prevent retailers who are not registered with the Department from purchasing products from wholesalers. The registration or resale number issued by the Department is required in order to assure the wholesaler that the business to which he sells is properly registered with the Department, which can then look to the retailer to collect and pay the tax required on retail sales. If a wholesaler fails to cooperate with this collection scheme by selling his product to a retailer without requiring proof under section 1 of a registration or a resale number, the wholesaler may expose himself to payment of the taxes the retailer incurred for sales at retail.

Tri-America Oil Co., 102 Ill. 2d at 238.

Because Tri-America was engaged in the business of selling tangible personal property at wholesale and retail, the court concluded that section 2c:

> require[d] it to obtain a resale tax certificate number from

> purchasers who purportedly intend[ed] to resell the product they purchase. If a purchaser does not have a resale number and therefore cannot comply with the requirements of section 2c by certifying to the seller who is operating as both a wholesaler and retailer that the sale is nontaxable for purposes of the Act, that sale is to be treated as a retail sale.

Id. at 239.

Next, Tri-America argued that even if it were a retailer required to comply with section 2c, it nevertheless rebutted the presumption imposed by section 4 of the ROTA, because it was undisputed that the unregistered gas station owner resold the gasoline to others for use or consumption. Tri-America Oil, 102 Ill. 2d at 240. The supreme court rejected that argument also, giving the following reasons:

> That argument misreads both section 4 [of the ROTA] and the decisions in *Dearborn Wholesale Grocers* and *Illinois Cereal Mills*. Section 4 of the Act states only that the "return so corrected *** shall be prima facie correct and shall be prima facie evidence of the correctness of tax due." [citation omitted] Section 2c, on the other hand, provides a method whereby a seller can avoid paying a retailers' occupation tax on sales it makes to others, sales which might otherwise be taxable as retail sales even though they may not in fact be retail sales. *The presumption raised by section 4 is thus not that a given sale is a sale at retail, but is rather that tax is due in the amount indicated by the Department. The presumption is rebutted, not by evidence that certain sales were made for resale, but either by a showing of compliance with section 2c or by a showing that section 2c does not apply.*

Tri-America Oil Co, 102 Ill. 2d at 240.

Here, "XYZ" does not dispute that it is a retailer. "XYZ"'s retailers' occupation tax returns were filed every month during the audit period, and those returns are part of the record in this case. Department Ex. 4. Nor does "XYZ" deny that it has not collected and maintained exemption certificates from its purchasers regarding the transactions at

issue. Tr. p. 62 (John Doe). The number of sales "XYZ" claimed as being for resale during the audit period was substantial (*see* Table 5, *supra*, p. 15), and such transactions were regularly made to the same persons. *See* Stip. Ex. 2. Since "XYZ" is engaged in the business of selling tangible personal property at retail, it has not established that section 2c does not apply to it. Tri-America Oil Co., 102 Ill. 2d at 240-41. Because "XYZ" has not complied with the requirements of section 2c regarding the disputed transactions, it has not rebutted the presumption that the gross receipts from such transactions at issue are subject to ROT. *See id.*

And even if the holding in the Tri-America decision had not clearly rejected "XYZ"'s argument regarding the type of proof necessary to support a claim that certain sales were sales for resale, only one of "XYZ" purchasers, in fact, fell within the classification of a "reseller" as described by the Illinois legislature in section 2c of the ROTA, and as opposed to one who purchases for "use", as defined in section 2 of the Use Tax Act ("UTA"). 35 **ILCS** 105/2. The Department gave full credit to "XYZ" regarding the transactions between it and the purchaser the Department's auditor determined was engaged in business as an art gallery. Department Group Ex. 2, pp. 4-7. The invoice prices of the transactions between "XYZ" and that registered reseller, therefore, were excluded from the global taxable exceptions scheduled regarding the disputed transactions.

While "XYZ" urges that the disputed transactions must be considered sales for resale because they cannot have been sales for use or consumption, it ignores the Illinois General Assembly's definition of "use" in favor of its own definition of the term. *See* "XYZ"'s Brief, pp. 10-11; "XYZ"'s Reply, pp. 6-8. The UTA's definition of "use"

complements the ROTA's definition of a reseller. *See* Chicago Tribune Co. v. Johnson, 119 Ill. App.3d 270 (1983) (since the UTA is *in pari materia* with the ROTA, both should be read together); 35 **ILCS** 120/2c (a reseller is "a purchaser … who claims to be a reseller of … tangible personal property in such a way that such resales are not taxable under this Act or under such other tax law which the Department may administer").

Section 2 of the UTA defines "use" as:

> the exercise by any person of any right or power over tangible personal property incident to the ownership of that property, *except that it does not include the sale of such property in any form as tangible personal property in the regular course of business* to the extent that such property is not first subjected to the use for which it was purchased ....

35 **ILCS** 105/2 (emphasis added).

The exclusion detailed in the second clause of the UTA's definition of "use" identifies the act of *selling* property purchased, in any form, *in the regular course of [the purchaser's] business*. Clearly, what the Illinois General Assembly intended to exclude from use taxation were the rights or powers over tangible personal property exercised by purchasers who were wholesalers, retailers, manufacturers, etc. – in effect, purchases by members of the class who might ordinarily "claim[] to be a reseller of … tangible personal property in such a way that such resales [would not be] taxable under this Act or under such other tax law which the Department may administer …." 35 **ILCS** 120/2c.

In this way, the legislature intended to place, for example, art collectors and art dealers into different classifications for Illinois tax purposes. The dealer, being engaged in the business of making sales of tangible personal property at retail, is subject to retailers' occupation tax for that privilege, while the collector is subject to use tax for the privilege of using tangible personal property purchased at retail. So, while the dealer and

collector might well engage in identical acts vis-à-vis their ownership of an item of tangible personal property (for example, purchasing a painting and directing others to hang it on a particular wall), the legislature intended each to be treated differently for purposes of the particular tax statutes affecting them.

Since the act of selling tangible personal property in the regular course of business is excluded from the definition of "use," the dealer would not be subject to use tax if it purchased and directed someone to hang a painting on a wall in a gallery, or in its warehouse for storage as inventory, or if it otherwise held the painting out for sale. The retailer, however, would owe ROT as measured by the gross receipts it received when it eventually sold the painting.

In contrast, the art collector would be subject to use tax if he purchased a painting at retail and directed others to hang it on a wall in Illinois. Tax, as measured by the collector's purchase price of the painting, would be due even if the collector directed or allowed others to hang the painting on a wall belonging to someone else, and even if the collector lived in a state other than Illinois. The collector's exercise of such powers, incidental to his ownership of the painting, is what the legislature intended to include within the definition of "use" as set forth in the UTA. 35 **ILCS** 105/2. Under those circumstances, tax would be due even if the collector never took the painting home and admired it while listening to music and sipping wine, as Mr. "XYZ" concluded was the only way to "use" artwork. Tr. p. 53 (John Doe). The collector, however, would not be subject to ROT if he eventually sold the work, because that subsequent transfer would

ordinarily constitute an occasional sale, which is not subject to ROT.[8] 35 **ILCS** 120/1.

"XYZ" has not rebutted the presumption that the disputed transactions were sales at retail (35 **ILCS** 120/1, 120/2c), and that the receipts therefrom were properly subject to tax. 35 **ILCS** 120/4; Tri-America Oil Co., 102 Ill. 2d at 240. "XYZ" has not supported its claim that the disputed transactions were sales for resale.

Conclusion:

"XYZ" did not introduce documentary evidence to show that it treated the monies identified in the invoices and consignment agreements like, respectively, loan receipts and interest payments. The documents of record show, instead, that "XYZ" treated the invoice amounts from the disputed transactions as receipts from sales of tangible personal property. "XYZ" did not introduce credible evidence, consistent with its books and records, to show that the disputed transactions were undertaken pursuant to unwritten loan agreements.

Because "XYZ" sells at both retail and at wholesale, it was required to support its claims that certain sales were for resale with documents conforming to section 2c of the ROTA. Since "XYZ" did not provide documents conforming to § 2c, it has not rebutted

[8] If, however, the collector habitually sells the tangible personal property he has collected, he may well place himself within the class of persons required to register pursuant to the provisions of the ROTA and the UTA. 35 **ILCS** 120/2a; 35 **ILCS** 105/2 (¶ 1 of the definition of a "Retailer maintaining a place of business in this State"). Considering the frequency with which many of the transacting parties engaged "XYZ" to act as their agent to sell, in Illinois, the paintings consigned (*see* Department Ex. 2, pp. 1-15 (names of transacting parties to disputed transactions set forth in schedule of global taxable exceptions); Stip. Ex. 2, pp. 156-61, 165-230 (24 representative transactions with XXXX)), that point may well have been reached here. In that case, "XYZ"'s sales to the collectors here should be viewed just as the Illinois supreme court viewed Tri-America's sales to the unregistered reseller in that case — i.e, taxable unless made in compliance with § 2c. Tri-America Oil Co., 102 Ill. 2d at 238-39.

the *prima facie* correctness of the Department's determination that tax was due in the amount set forth in the correction of "XYZ"'s returns.

Therefore, I recommend the Director finalize Notice of Tax Liability no. SF-19950000000000 as issued, with interest to accrue pursuant to statute.

Date Issued	Administrative Law Judge